

DOCKET FILE COPY ORIGINAL

1401 H Street, N.W.
Suite 1020
Washington, D.C. 20005
Office 202/326-3822



Anthony M. Alessi
Director
Federal Relations

May 6, 1994

EX PARTE OR LATE FILED

RECEIVED

MAY 6 1994

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, NW
Room 222
Washington, DC 20554

RE: Ex Parte Statement
Docket No. 93-179

Dear Mr. Caton:

On May 6, 1994, Mr. Daniel J. Fling, Director - Federal Regulatory Policy, Mr. David Sorenson, Manager - Price Caps of Ameritech and I met with Mr. Gregory Vogt, Chief, and Mr. David Nall, Deputy Chief, of the Tariff Division to discuss Ameritech's position in the above referenced proceeding. The attached information was used as the basis for our discussion.

Sincerely,

A handwritten signature in black ink, reading "Anthony M. Alessi". The signature is written in a cursive, flowing style.

Attachment

cc: G. Vogt
D. Nall

No. of Copies rec'd 0+2
List A B C D E



AMERITECH'S POSITION AGAINST ADD-BACK OF SHARING

- **ADD BACK HAS NO PLACE IN PRICE CAP REGULATION**

- The differences between sharing and refunds under ROR regulation are clear:

Refunds:

- * Result from rate of return, cost-plus regulation
- * Are retrospective in nature
- * Indicative of past unlawful rates
- * Exclude earnings from interexchange services
- * Amount refunded is unaffected by future demand

Sharing:

- * Results from incentive regulation
- * Is prospective in nature
- * Is a means of sharing productivity achievements
- * Results from a lawful rate structure
- * Includes earnings from interexchange services
- * Total amount shared is affected by future demand
- * Reduces price ceilings but does not necessarily result in a dollar-for-dollar reduction in rates (if prices are below the ceiling)

The Commission itself stated in the NPRM (93-179) that, since sharing is not a refund, parties might well argue that the appropriate measure of sharing is a price cap carrier's "actual" earnings (i.e., without add-back).

- Add-back further diminishes the efficiency incentives envisioned for price cap regulation, because add-back reduces the retained rewards of efficiency improvements.
- With add-back, sharing is nothing more than a refund, and price caps look like rate of return regulation with a range of permitted returns.

*AMERITECH'S POSITION AGAINST ADD-BACK OF SHARING
(CONT.)*

- Add-back causes contradictions with intended mechanics of sharing:
 - * The Commission has made it clear that sharing was to be regarded as "one-time reduction in the PCI for the next rate period", and that 50% of earnings between 12.25% and 16.25% are shared. (Second Report and Order, CC Docket No. 87-313, released October 4, 1990, paras. 124, 136)
- Add-back can result in sharing well beyond the one-year period, and the amount shared will greatly exceed 50%.
- * Attachment 1 provides an example that demonstrates both of these contradictions resulting from add-back.

Assume, in year 1 an LEC earns over 12.25%, resulting in sharing in year 2.

Also assume that actual rates of return in years 2 and beyond are just at 12.25%.

Add-back would raise year 2's reported rate of return above 12.25%, resulting in sharing in year 3. This in turn will raise year 3's rate of return into the sharing range. This could continue indefinitely into the future.

The results in sharing of year 1's earnings for many years into the future, not just the next 12 months.

50% of year 1's earnings are shared in year 2. Then due to add-back, a portion of year 1's earnings would be shared in years 3, 4, and beyond. Added together, much more than 50% of year 1's earnings above 12.25% would be shared over subsequent years.

AMERITECH'S POSITION AGAINST ADD-BACK OF SHARING

ATTACHMENT 1

	<u>Return</u>	<u>Investment</u>	<u>ROR(%)</u>	<u>Return above 12.25%</u>	<u>50% of Return above 12.25%</u>	<u>Sharing Amount (w/gross-up)</u>
Year 1	\$382.5	\$3000	12.75	\$15	\$7.5	\$11.5
Without add-back:						
Year 2	367.5	3000	12.25	0	0	0
Year 3-10	367.5	3000	12.25	0	0	0
With add-back:						
Year 2	379.0 (367.5+11.5)	3000	12.63	11.5	5.8	8.9
Year 3:	376.4 (367.5+8.9)	3000	12.55	8.9	4.4	6.8
Year 4	374.3	3000	12.48	6.8	3.4	5.3
Year 5:	372.8	3000	12.43	5.3	2.6	4.0
Year 6:	371.5	3000	12.38	4.0	2.0	3.1
Year 7:	370.6	3000	12.35	3.1	1.6	2.4
Year 8:	369.9	3000	12.33	2.4	1.2	1.8
Year 9	369.3	3000	12.31	1.8	0.9	1.4
Year 10	368.9	3000	12.30	1.4	0.7	1.1
Sum of Years 1-10:					\$30.1	
% of year 1's return shared (30.1/15)=					200.7%	

This example shows that add-back results in the sharing of year 1's earnings through year 10 and beyond (not just year 2), and that over 200% (not 50%) of year 1's return above 12.25% is shared during this period.